

## Message Text

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ACTION EA-09

INFO OCT-01 EUR-12 ISO-00 AID-05 CIAE-00 COME-00 EB-07

FRB-03 INR-07 NSAE-00 USIA-06 TRSE-00 XMB-02 OPIC-03

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INFO AMEMBASSY LONDON

AMEMBASSY PARIS

AMEMBASSY ROME

AMEMBASSY SEOUL

USMISSION OECD PARIS

USMISSION USEC BRUSSELS

C O N F I D E N T I A L TOKYO 17965

E.O. 11652 GDS

TAGS: EGEN, JA

SUBJ: JAPANESE ECONOMY AT YEAR END

REF: TOKYO 16739

SUMMARY. SOME PESSIMISTIC ESTIMATES FOR THE JAPANESE ECONOMY  
RECENTLY RELEASED SEEM EXAGGERATED. NON-GOVERNMENT DEMAND WILL  
PROBABLY BE SUFFICIENT TO MAINTAIN GRADUAL RECOVERY AND  
INCREASED GOVT SPENDING TO PROVIDE FURTHER STIMULATION IS  
EXPECTED. SOME SECTORS SUCH AS STEEL WILL BE SLOWER TO REVIVE  
BECAUSE OF LARGE INVENTORIES AND IDLE PRODUCTIVE CAPACITY.  
DIET APPROVED PRICE RISES FOR TOBACCO AND LIQUOR WILL RAISE  
THE CPI BY ABOUT 0.7 PCT BUT WILL OTHERWISE HAVE LITTLE  
EFFECT. END SUMMARY.

1. A NUMBER OF RECENT ESTIMATES OF JAPANESE ECONOMIC  
PROSPECTS HAVE BEEN APPRECIABLY MORE PESSIMISTIC IN THE  
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LAST FEW WEEKS. FOR EXAMPLE, JAPAN ECONOMIC RESEARCH

CENTER (JERC) NOW PREDICTS REAL GROWTH IN JFY 1975 AT 1.3 PERCENT, CONSIDERABLY BELOW THE GOJ ESTIMATE OF 2.2 PERCENT WHICH ITSELF WAS A DOWNWARD REVISION. ALTHOUGH PREVIOUSLY IT HAD SEEMED TO US THAT ESTIMATES, ESPECIALLY FROM THE GOJ, WERE OVERLY FAVORABLE BECAUSE FINAL DEMAND WAS NOT RISING ENOUGH TO KEEP PACE WITH THE PRODUCTION UPSWING WHICH DID OCCUR IN THE APRIL TO AUGUST PERIOD, WE NOW CAUTION AGAINST BEING TOO PESSIMISTIC.

2. SLOW RECOVERY IS CONTINUING. ALTHOUGH EXPORTS DECLINED IN NOVEMBER, THERE ARE REPORTS THAT EXPORT ORDERS ARE INCREASING AND THAT HOLIDAY SEASON SALES BY DEPARTMENT STORES ARE HIGHER THAN ANTICIPATED. INCREASES IN PRODUCERS SHIPMENTS AVERAGED 1.66 PERCENT IN THE PAST TWO MONTHS. NONE OF THESE CAN BE TAKEN AS FULLY RELIABLE LEADING INDICATORS, BUT THEY ARE SIGNS THAT THE ECONOMY CONTINUES TO MOVE AHEAD.

3. THE MAJOR IMPETUS FOR RECOVERY WILL HAVE TO COME FROM THE GOVERNMENT SECTOR. THE MUCH-PUBLICIZED FOURTH RECOVERY PLAN WAS ENACTED BY THE DIET ONLY ON NOVEMBER 7 AND IS JUST BEGINNING TO PRODUCE NEW GOVERNMENT SPENDING. COMBINED WITH THE REGULAR BUDGET DEFICIT, NATIONAL AND LOCAL GOVERNMENTS ARE EXPECTED TO FINANCE A TOTAL OF ABOUT DOLS 38.6 BILLION IN BONDS. NOT ALL OF THAT RESULT IN NEW DEMAND, BUT IS SIGNIFICANT THAT EARLY ESTIMATES FOR NEXT FISCAL YEAR ARE MUCH HIGHER--ABOUT DOLS 50 BILLION. AN ADDITIONAL SHOT IN THE ARM OF DOLS 11-12 BILLION IN GOVERNMENT SPENDING NEXT YEAR OUGHT TO HAVE MAJOR EFFECTS. IT SEEMS SAFE TO ASSUME THAT MOST OF THAT INCREMENT WILL BE TRANSLATED INTO NEW DEMAND AND THAT CONSUMER DEMAND, BUSINESS INVESTMENT AND EXPORTS WILL NOT DECLINE FROM PRESENT LEVELS. JERC ESTIMATES REAL GROWTH IN JFY 1976 WILL BE 4.6 PERCENT.

4. THE BUDGET FOR NEXT YEAR IS NOW IN PREPARATION, AND THERE WILL BE A HEAVY DEFICIT. HOW MUCH OF A DEFICIT IS PARTLY A POLITICAL VARIABLE AND PARTLY A PASSIVE  
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RESULT OF REDUCED REVENUE. HOWEVER, EVEN CONSERVATIVES IN THE FUKUDA CAMP SEE NO MAJOR RISK OF INFLATION, AND DIET ELECTIONS NEXT YEAR OUGHT TO ENCOURAGE THE CABINET TO MAKE EXPANSIONARY ECONOMIC DECISIONS. IT IS INTERESTING TO NOTE THAT THE MOST POPULAR ARGUMENT AGAINST ALLOWING A BIG DEFICIT IS THAT GOVERNMENT WOULD PREMPT FINANCIAL MARKETS AND HOLD DOWN BUSINESS INVESTMENT. THE ASSUMES THAT BUSINESS WANTS TO INVEST AND THAT

MONETARY AUTHORITIES WILL NOT ALLOW CREDIT EXPANSION. MORE BUSINESS INVESTMENT WOULD BE WELCOME, BUT IT SHOWS NO SIGNS OF REVIVING, AND MONETARY EAST WILL PROBABLY CONTINUE FOR SOME TIME.

5. THE UPWARD STRUGGLE, HOWEVER, WILL BE DIFFICULT IN SOME RESPECTS THE JAPANESE RECESSION IS SHOWING SIGNS OF STIFFNESS BECAUSE IDLE LABOR AND PRODUCTIVE CAPACITY IN PLANTS WILL HAVE TO BE PUT BACK TO WORK BEFORE PRIVATE SECTOR INVESTMENT REVIVIES. IN RECENT WEEKS, FOR EXAMPLE, BASIC IRON AND STEEL PRODUCTION HAS BEEN CUT BECAUSE OF EXCESSIVE INVENTORIES. THE STEEL INDUSTRY WILL BE RELUCTANT TO REFIRE FURNACES UNLESS DEMAND RECOVERS STRONGLY. OTHER SECTORS ARE IN A SIMILAR POSITION WITH BOTH WORKERS AND PRODUCTION LINES ON HAND BUT IDLE.

6. ON DECEMBER 13 THE DIET PASSED BILLS TO RAISE PRICES OF TOBACCO AND TAKES OF LIQUOR. THIS ACTIONS WILL CAUSE A RISE IN THE CONSUMER PRICE INDEX OF ABOUT 0.7 PCT. BUT THE DIRECT ECONOMIC IMPACT WILL BE INSIGNIFICANTLY. THE PRICE CHANGES WILL NOT GREATLY ALTER CONSUMER PURCHASING AND THEINCREASED GOVERNMENT REVENUES WILL BE SPENT.

7. WE CONCLUDE THAT PREVAILING PESSIMISTIC EXPECTATIONS ARE EXAGGERATED, BUT THATTHEY ARE GENERATING PRESSURES FOR A MORE FORCEFUL POLICY OFGOVERNMENT SPENDING TO STEP UP THE PACE OF GRADUAL RECOVERY.  
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